



# **Department of Defense Utilities Privatization Program**

## **Responses to Industry Questions** *September 29, 2004*

**Captain Rick Marrs**  
**Office of the Deputy Under Secretary of Defense**  
**(Installations and Environment)**



# Government Panel Members

---

AT&L / Installations & Environment

**CAPT Rick Marrs**, *DoD Utilities Privatization Program Manager,  
Office of the Deputy Secretary of Defense (Installations & Environment)*

**Jim Cotton**, *Director, Utility Privatization Program Manager,  
Energy Enterprise Office, Defense Energy Support Center*

**Greg Zagorin**, *Associate Counsel,  
Defense Energy Support Center*

**Rich Dubicki**, *Assistant for Utilities Privatization,  
Assistant Secretary of the Army (I&E) Privatization and Partnerships*

**Rob Kittel**, *Chief, Regulatory Law and Intellectual Property Division,  
U.S. Army Legal Services Agency*

**Ken Miller**, *Utilities Privatization Program Manager,  
Office of the Air Force Civil Engineer*

**Bill Kraynak**, *Utilities Privatization,  
Commander, Navy Installations*

**Bill McQuaid**, *Senior Program Examiner, National Security Division,  
Office of Management and Budget*



# Rules of Engagement

---

AT&L / Installations & Environment

- 1. This brief provides general comments on policy for future procurements.**
- 2. Some of the comments may require further explanation to be applied to specific procurements.**
- 3. The panel will not address specific issues for ongoing procurements.**
  - (Please refer to your Contracting Officer)
- 4. Resolution of privatization challenges is often case specific, especially if legal issues are involved.**



# Topic Areas

---

AT&L / Installations & Environment

- **Cost Accounting Standards (CAS)**
- **Fair Market Value**
- **Contribution in Aid of Construction (CIAC)**
- **Lesser Estate and Delayed Conveyance**
- **Communication and Timeliness**
- **Should Cost Estimate (SCE) and Economic Analysis**



# Cost Accounting Standards (CAS)

## Questions from Industry:

1. **What is the status of the potential CAS waiver for utilities privatization?**



# CAS Waiver Update

---

AT&L / Installations & Environment

- **The Cost Accounting Standards Board has granted DoD the authority to waive CAS for utilities privatization contracts when certain conditions exist**
- **Implementing guidance is anticipated to be issued around 15 Oct 2004**
- **Further information will be promulgated**



# Fair Market Value (FMV)

## Questions from Industry:

- 1. What is DoD policy for determining FMV of utility systems?**
- 2. Is there a consistent approach for determining FMV?**
- 3. Why are some contracting officers encouraging FMV of \$1 while others expect replacement cost new less depreciation (RCNLD)?**
- 4. Is FMV open for negotiations?**
- 5. To what extent must the proposed purchase price match the FMV?**
- 6. Can the proposed purchase price exceed FMV?**



# Fair Market Value (FMV) Overview

AT&L / Installations & Environment

- **10 USC 2688 requires consideration for the conveyance**
  - “equal to the fair market value (as determined by the Service Secretary)”
- **“As is value” (FMV) is a key element of each proposal**
  - Foundation for book value which contributes to rate base
  - Recapitalization and depreciation based on book value after upgrades
- **Some utilities are concerned about balance sheet impact of booking a liability for FMV**





# Service Policy for Determining FMV

AT&L / Installations & Environment

- **Government estimates a range of FMV (using consultant)**
  - Higher Limit: Replacement Cost New Less Depreciation (RCNLD)
  - Lower Limit: Original Cost New Less Depreciation (OCNLD)
  - Obsolescence and other reasonable factors are considered
- **Elements of RCNLD open for negotiation**
  - Contracting Officers should ensure open discussions
  - Specific aspects of proposed FMV should be addressed
  - Well documented, actual market prices should be considered
- **Army has previously allowed use of nominal value**
  - Must be fully justified by business case



# Suggested Resolution of FMV Issues

---

AT&L / Installations & Environment

- **Establish FMV through open negotiations**
- **Contractor will recover FMV through service contract**
- **Contractor will earn a reasonable return on investment**
- **CIAC implications addressed as separate issue**



# Contribution In Aid of Construction (CIAC)

## Questions from Industry:

1. **What is DoD policy regarding how CIAC is handled?**
2. **Is DoD pursuing a FAR deviation to allow the recovery of CIAC related Federal income taxes?**
3. **Will DoD be responsible for CIAC related taxes, penalties and interest resulting from FMV disagreements with IRS?**
4. **If CIAC related taxes are not recoverable, will only tax exempt entities be competitive in utilities privatization procurements?**



# Potential FAR Deviation for CIAC

AT&L / Installations & Environment

- **Per FAR Part 31.205-41 – Taxes, Federal income taxes are not an allowable cost**
- **FAR Part 31 applies to the pricing of contracts when cost analysis is performed and when reimbursement is based on actual costs incurred**
- **A deviation is being considered to allow CIAC related Federal income taxes under certain conditions on future contracts**
- **Anticipate implementing guidance to be issued in Oct 2004**
- **Details will be promulgated**



# Lesser Estate and Delayed Conveyance

## Questions from Industry:

- 1. Is a capital lease or other lesser interest an acceptable alternative for privatization?**
- 2. What is DoD policy for delayed conveyance?**
- 3. What is DoD policy in allowing lesser estate?**



# DoD Policy for Title Transfer

AT&L / Installations & Environment

- **Privatization with full title transfer is the Department's preferred method**  
“In order to effectuate privatization of the utility system (as opposed to outsourcing utility system operation and maintenance) the Military Department must convey all rights in the asset.”  
*DoD Guidance for Privatizing Utility Systems, II-C-1, page 3*



# “Lease to Own” Authority

AT&L / Installations & Environment

- **Lease to own or delayed conveyance is allowable**

“....if the [Service] Secretary concerned determines that delayed transfer of title is economically preferable to an immediate transfer of title, the Secretary may structure the conveyance as a lease-purchase or a lease in furtherance of conveyance, as long as the non-federal entity at some point takes title to the asset.”

*DoD Guidance for Privatizing Utility Systems, II-C-1, page 3*

- **Delayed conveyance has been successful**



# Benefits of Delayed Conveyance

---

AT&L / Installations & Environment

- **Delayed conveyance allows Contractor to perform critical due diligence and system upgrades prior to assuming ownership**
  - Further assess need for system upgrades and associated costs
  - Comply with safety/environmental requirements
  - System inventory tagging/mapping
  - Achieve industry standard operating conditions
- **Due diligence/system assessment provides Government with more accurate upgrade costs**
- **Reduced risk of ownership should result in better deal for the Government and the Contractor**





# DoD Policy for Lesser Estate

AT&L / Installations & Environment

- **If privatization with full title transfer is determined to be uneconomical and the system is certified exempt by the Service Secretary, leasing or other conveyance of lesser estate may be pursued**  
“In the event the Secretary concerned certifies the basis of an exemption, the Component is encouraged to pursue other innovative measures to improve operational efficiency.”

***DoD Guidance for Privatizing Utility Systems, II-B, page 2***



# Communication and Timeliness

## Questions from Industry:

- 1. Are common timelines and communication plans in place to negotiate and award contracts?**
- 2. Is there any directive to execute contracts by a certain date and hold government negotiation teams accountable?**
- 3. What is schedule and timing of upcoming RFPs?**
- 4. What are the remaining installations and systems awaiting RFP release and what is the schedule?**



# Communication and Timeliness

---

AT&L / Installations & Environment

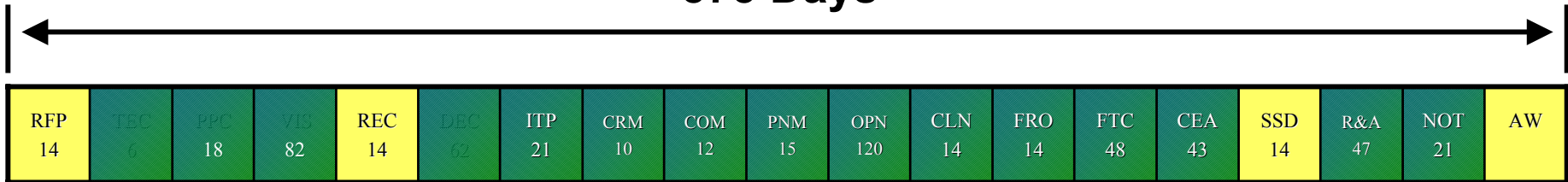
- **Contracting agencies are under a tight schedule**
- **Offerors have limited resources to respond to solicitations, amendments and negotiations**
- **Priority is to allow sufficient flexibility to achieve success through privatizing systems**
- **Contracting officers provide overall schedule of evaluation**
  - If the schedule slips over 30 days, the offerors are informed
- **Contracting officers keep offerors advised of the next step and when it will occur**



# Sample Timeline, DESC

AT&L / Installations & Environment

575 Days



**Timeline: RFP Issue thru Contract Award**

## Major Procurement Milestone Legend:

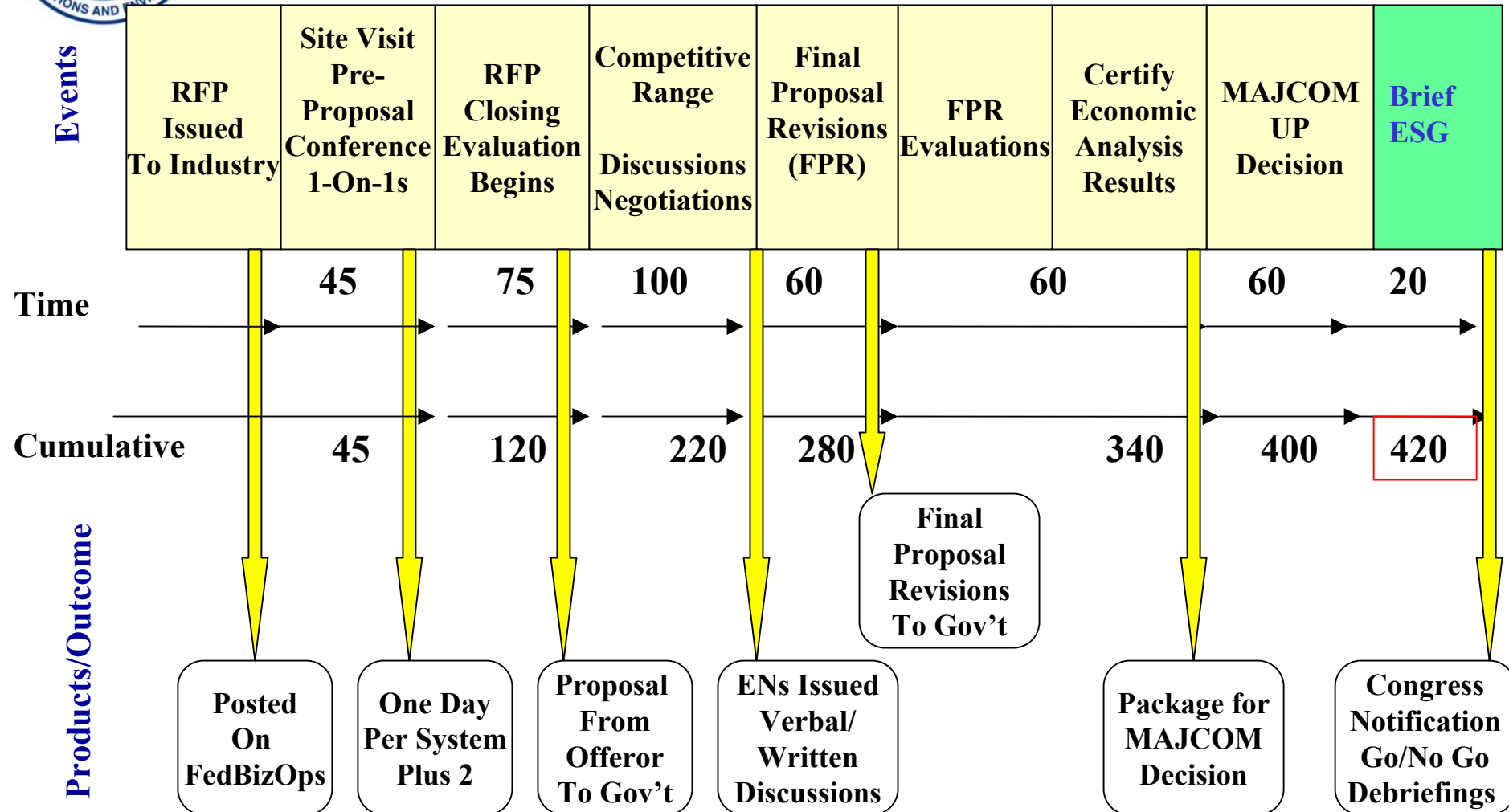
RFP – Issue Request For Proposal	ITP – Tech & Price Eval Reports Due	FTC – Complete Final Tech & Price Evals
TEC – Prepare Tech Library	CRM – Cost Realism Report Due	CEA – Complete Certified Econ Analysis
PPC – Pre-proposal Conf	COM – Competitive Range Determination	SSD – Source Selection Authority Decision
VIS – Site Visit	PBM – Sign Pre-negotiation Memo	R&A – Send Review & Approval Package
REC – Initial Proposals Due	OPN/CLN – Open/Close Negotiations	NOT – Congressional Notification
DEC – Evaluator Training	FRO – Final Revised Proposals Due	AW – Award Contract

**Note: Sample timeline for Defense Energy Support Center. Actual timelines may be different.**



# Sample Timeline, Space Command

AT&L / Installations & Environment



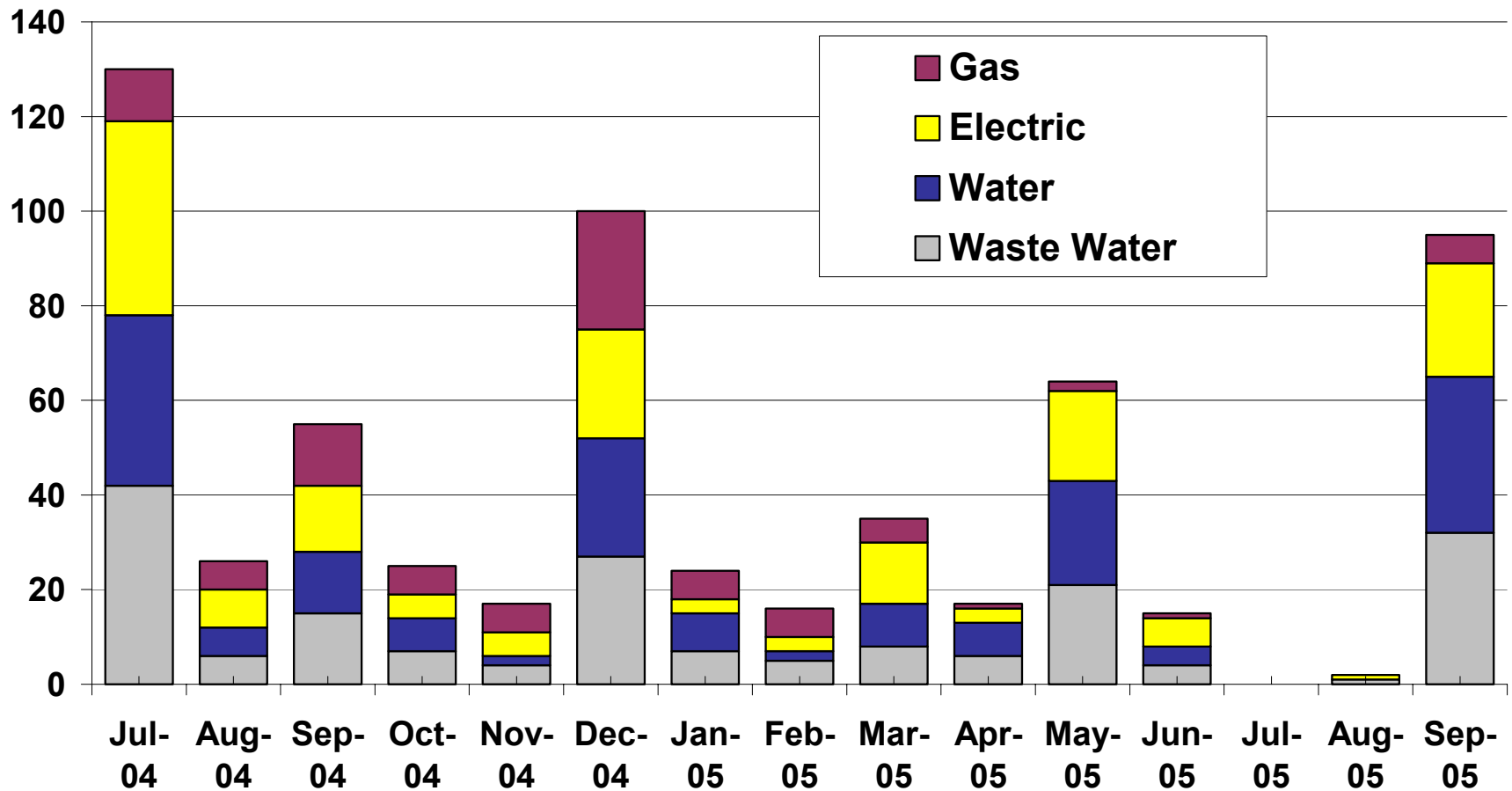
**Note: Sample timeline for U.S. Air Force Space Command. Actual timelines may be different.**



# SSA Decisions (Projected)

AT&L / Installations & Environment

*As of 06/30/04*





# Should Cost Estimate and Economic Analysis

## Questions from Industry:

- 1. What is DoD guidance for defining should cost?**
- 2. What is the government's economic analysis methodology?**
- 3. Is the Government performing a fair analysis?**
- 4. How is the government accounting for contributions/work effort from different departments/cost centers?**
- 5. How are differences in standards addressed in the economic analysis?**
- 6. Should a regulated utility be allowed to apply its internal standards (design, construction, etc.) in lieu of Government specifications?**



# Economic Analysis Guidance

---

AT&L / Installations & Environment

“The Defense Components shall use a benefit-cost analysis as described in OMB Circular A-94 to perform the economic analysis of each utility system, including net present value calculations to determine the life cycle costs and benefits of each proposal”

***DoD Guidance for Privatizing Utility Systems, IV-B, page 8***

“The Defense Components shall utilize the UPEAST analysis model ... or a comparable cost model to conduct the required life cycle analysis”

***DoD Guidance for Privatizing Utility Systems, IV-B-1, page 8***





# Development of Should Cost Estimate

AT&L / Installations & Environment

- **The Military Services use consultants to develop estimate**
  - Neutral third parties
  - Collect necessary information
- **System Inventory**
- **As-Is Condition and Fair Market Value**
- **Should Cost Estimate Components**
  - Operations & Maintenance
  - General & Administrative (25%)
  - Initial Capital Upgrades
  - Recapitalization



# Industry Standards Considerations

---

AT&L / Installations & Environment

- **Understand standards used in the preparation of the Government should cost estimate (SCE) and all proposals**
  - Recognize that each offeror may use a different standard
- **Determine/verify the government's required level of service**
  - Identify significant differences in standards
  - Adjust SCE, if a higher standard is required
- **Communicate with offerors**
- **Develop like comparison**
- **Understand remaining differences**



# Steps to Address Industry Standards

AT&L / Installations & Environment

- 1. Ensure the Should Cost Estimate is compliant with applicable industry, environmental, safety, fire and technical standards**
- 2. Offeror(s) should provide justification to deviate from applicable standards**
- 3. Ensure economic analysis reflects an “apples-to-apples” comparison**



# Points of Contact

AT&L / Installations & Environment

- **Office of Deputy Under Secretary of Defense (Installations and Environment)**
  - <http://www.acq.osd.mil/ie/irm/utilities/utilities.htm>
  - Captain Rick Marrs, CEC, USN (703) 697-6193
- **Army Assistant Chief of Staff (Installation Management)**
  - <https://www.pts.army.mil/>
  - Bob Sperberg (703) 601-0367
- **Department of the Navy**
  - <https://energy.navy.mil/privatization/> General UP info and current RFP's
  - <http://www.esol.navfac.navy.mil/> Solicitations
  - Commander Navy Installations- LCDR Roland de Guzman (202) 433-4504
  - Marine Corps- David Heinrichs (703) 695-9781
  - Naval Facilities Engineering Command Bill Tayler (202) 685-9254
- **Air Force Office of the Civil Engineer (Readiness & Installation Support)**
  - <http://www.afcesa.af.mil/ceo>
  - Ken Miller (703) 604-4304
- **Defense Energy Support Center (DESC) Utility Privatization Branch**
  - <http://www.desc.dla.mil/>
  - Jim Cotton (703) 767-8135
- **Federal Business Opportunities**
  - <http://www.fedbizopps.gov/>